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IN THE
Supreme Court of the United States
OCTOBER TERM, 1992

TWIN CITY FIRE INSURANCE CO., *et al.*,
Petitioners,
v.
SAMUEL F. FORTUNATO, COMMISSIONER OF THE NEW JERSEY DEPARTMENT OF INSURANCE,
Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of New Jersey

BRIEF OF AMERICAN INSURANCE ASSOCIATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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QUESTIONS PRESENTED

1. Is the right to withdraw from a regulated market a protected liberty interest under the Due Process Clause as a safeguard against oppressive state regulation?

2. Does the unconstitutional conditions doctrine prohibit a state from conditioning the right to withdraw from an unprofitable business on forfeiture without compensation of valuable property interests in unrelated businesses?

3. Should the prohibition on protectionist state insurance taxes in *Metropolitan Life Ins. Co. v. Ward*, 470 U.S. 869 (1985), be applied to state insurance laws that protect local markets and discriminate against interstate commerce by imposing onerous penalties on an insurer's withdrawal from the state?

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BRIEF OF AMERICAN INSURANCE ASSOCIATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

INTEREST OF THE *AMICUS CURIAE*

Amicus curiae American Insurance Association ("AIA") is a trade association whose member insurers write property and casualty insurance throughout the United States, amounting to approximately 25% of such insurance sold in this country.[1] Many AIA members also write property and casualty insurance in New Jersey, including approximately 19 percent of the auto insurance sold in that state.

In recent years, certain lines of insurance—particularly auto and workers' compensation—have become unprofitable in some states due to escalating claims costs, accompanied by the refusal of those states' regulators to permit rate increases sufficient to recoup those higher costs. As a result, many AIA members have withdrawn

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[1] Petitioners and respondent have consented to the filing of this brief. Copies of the parties' consent letters have been filed with the Clerk.

from these unprofitable lines and committed their capital to more efficient uses in insurance markets in other states.

The decision of the New Jersey Supreme Court in this case, however, sanctions application of a law to effectively prohibit AIA members from withdrawing from New Jersey's loss-ridden auto insurance market by threatening confiscation of the insurers' other property and casualty businesses in New Jersey if they leave. The lower court's decision thus deprives AIA's members of the freedom to relocate their businesses within interstate commerce and conscripts them into subsidizing local markets out of the pockets of their shareholders and customers in other states.

Due to the significant impact of the New Jersey law on its members, AIA participated as an *amicus curiae* in this case both before the Appellate Division of the New Jersey Superior Court and before the New Jersey Supreme Court.

REASONS FOR GRANTING THE WRIT

INTRODUCTION AND SUMMARY OF ARGUMENT

This case presents significant constitutional issues concerning a state's power to prevent businesses from withdrawing from regulated markets. Petitioners challenge New Jersey's revocation of their non-automobile insurance licenses as a coercive device to prevent them from withdrawing from the New Jersey automobile insurance market. The forfeiture of those non-auto licenses was not to protect New Jersey policyholders from the disruptive effect of sudden withdrawal from the auto insurance market; that legitimate regulatory interest was addressed by other regulatory measures, such as a transition period for withdrawal, which are not challenged here. Rather, the purpose of revoking petitioners' licenses, as expressed by the Insurance Commissioner and the court below, was to deter auto insurers from leaving the state *at all* and thus to compel them to assume unprecedented regulatory burdens.

In 1990, New Jersey fundamentally changed its regulation of the private passenger automobile insurance market by enacting the Fair Automobile Insurance Reform Act ("FAIR Act"). The new law took the radical step of, in effect, transforming private insurers into public utilities with a common carrier obligation to take on all customers, except those with the very worst driving records. The new act also imposed on insurers the obligation of paying off the massive deficit, exceeding $3 billion, incurred by the state-administered mechanism for underwriting automobile drivers unable to obtain coverage from private insurers.

To coerce insurers into asuming these onerous new regulatory burdens, § 72 of the FAIR Act authorized the Commissioner of Insurance to require any insurer withdrawing from the automobile market, and all of its affiliates, to forfeit their licenses to engage in any other type of property and casualty insurance business. *See* N.J. Stat. Ann. § 17:33B-30 (reprinted at Pet. App. A-57). This provision has widely been characterized as a "lock-in" law because the threat of losing profitable non-automobile insurance businesses effectively compels insurers to remain in the automobile market.

New Jersey's threat to confiscate an insurer's valuable property interests, to compel acquiescence in new regulatory burdens imposed in an entirely separate market, presents important constitutional issues:

1. "Lock-in" laws deprive a regulated business of its remedy of last resort against oppressive regulation—withdrawal from the regulated market. Exit barriers are thus a highly effective instrument of regulatory coercion designed to force businesses to submit to burdens that no company would shoulder voluntarily. In this case, for example, New Jersey has compelled insurers to capitulate to regulatory mandates substantially depriving them of their underwriting freedom and making them pay off deficits that the state had, only a few years before, statutorily

promised they would never have to assume. The decision of the New Jersey Supreme Court thus sends a signal to other states that they, too, can enact regulatory schemes requiring subsidization of local markets without fear that insurers will be able to depart the jurisdiction for states with more balanced regulatory environments.

In contrast to the decision of the New Jersey Supreme Court, the lower federal courts have regarded the right of market exit as so important a safeguard against restrictive regulation that the opportunity for withdrawal has frequently been cited in sustaining the constitutionality of regulatory laws, such as those in New Jersey, that severely restrict a company's return on investment. This Court should resolve this conflict between state and federal courts on whether regulated companies have a liberty interest in market exit protected under the Due Process Clause, especially in response to changes in the regulatory regime that upset a company's investment-backed expectations.

2. This case also presents a second significant question concerning the constitutional reach of a state's power to hold companies captive to a local market. That question is whether the constitutional conditions doctrine prohibits a state from threatening confiscation of one regulated business in order to prevent companies from leaving an entirely distinct market having no nexus whatsoever to the business being seized.

Acknowledging the fact that different lines of insurance are economically separate markets, New Jersey has always treated the automobile and non-automobile insurance businesses as unrelated ones for regulatory purposes. Entry into one market is not conditioned on entry into another, certificates of authorization to underwrite particular lines are separately issued, and rates are set separately for each market. The only legal or factual linkage between these different markets is the Commissioner's finding that the threatened seizure of profitable non-automobile insurance businesses will "encourage"

automobile insurers to remain in the state. Pet. App. A-87.

In effect, the Commissioner is using the fortuity of his power over a profitable unrelated business to advance regulatory interests that are wholly unconnected to the insurance licenses he has threatened to revoke. This Court has strongly suggested that such linkage is nothing but "an out-and-out plan of extortion." *Nollan v. California Coastal Comm'n*, 483 U.S. 825, 837 (1987). *Nollan*, however, was decided in the context of a threatened confiscation of property that did not substantially advance the asserted state regulatory interest. Here, the threatened seizure of insurers' non-auto insurance businesses all too effectively advances New Jersey's illegitimate interest in holding auto insurers captive to the state. The Court should thus consider whether *Nollan* applies where a regulator attempts to advance state interests in one market by imposing a confiscatory condition on property held in an entirely separate business.

3. The petition should also be granted to resolve a conflict among the highest courts of three states over the constitutionality of insurance "lock-in" laws. The Massachusetts Supreme Judicial Court has upheld the constitutionality of a "lock-in" provision closely similar to the New Jersey statute. *See Maryland Casualty Co. v. Commissioner of Ins.*, 363 N.E.2d 1087 (Mass. 1977). However, a decision by the North Carolina Supreme Court struck down a "lock-in" law on the basis of the unconstitutional conditions doctrine and thus squarely conflicts with the decisions in Massachusetts and New Jersey. *See Hartford Accident & Indem. Co. v. Ingram*, 226 S.E.2d 498 (N.C. 1976).

4. A third significant question presented by the decision below is whether the states have a legitimate regulatory interest, under the Due Process Clause, in erecting market exit barriers intended to conscript insurers to serve local markets at the expense of out-of-state businesses and policyholders. "Lock-in" laws are inherently

protectionist. The New Jersey statute effectively prohibits multi-line insurers from transferring their capital, human and other resources committed to the New Jersey automobile insurance market to other insurance markets in interstate commerce. Further, because New Jersey's automobile insurance business has been unprofitable for many years, the effect of the New Jersey statute is to require out-of-state interests—insurer businesses in states other than New Jersey, and out-of-state policyholders—to subsidize the New Jersey market.

In *Metropolitan Life Insurance Co. v. Ward*, 470 U.S. 869 (1985), this Court determined that, notwithstanding the McCarran-Ferguson Act, 15 U.S.C. §§ 1011-15, state insurance taxes intended to promote domestic insurance businesses, by discriminating against out-of-state businesses, serve no legitimate state interest under the Equal Protection Clause. This case should be reviewed to determine whether the prohibition against protectionist state taxation in *Metropolitan Life* should be applied to other types of protectionist insurance laws.

I. THE DECISION BELOW IS INCONSISTENT WITH FEDERAL COURT DECISIONS RECOGNIZING THAT THE RIGHT TO WITHDRAW FROM A MARKET IS AN ESSENTIAL SAFEGUARD AGAINST OPPRESSIVE REGULATION.

The takings and due process issues presented by this case warrant review because they implicate the ultimate constitutional safeguard against onerous state regulation —the right to get out of the regulated business.

New Jersey's Commissioner of Insurance forthrightly has said that the state's "lock-in" law is intended to coerce insurers into bearing the unprecedented regulatory burdens imposed by the FAIR Act, by threatening them with loss of their non-auto business if they seek to withdraw from the automobile insurance market. *See In re Fireman's Fund Ins. Co.*, Ins. Dept. No. 891-320 (Sept.

17, 1991) at 3 (requiring an insurer and its affiliates to forfeit all non-automobile property and casualty licenses in order to deter withdrawals and thus preserve the "comprehensive reforms wrought by the FAIR Act").

Because New Jersey's "lock-in" law has a manifestly coercive purpose, commentators have aptly described it as "a form of regulatory blackmail to prevent insurers from withdrawing from the auto insurance market." J.D. Cummins & M.A. Weiss, *Regulation and the Automobile Insurance Crisis*, Regulation, Spring 1992, at 52. "Most insurers are not auto insurance specialists but rather write various types of insurance," including commercial property and casualty coverages from which they derive "[a] high proportion of [their] revenues." *Id.* As a result, if New Jersey carries out its threat "to cancel the insurer's licenses to write all types of coverage in the state . . . the insurers would have to give up profitable commercial writings to leave the auto market." *Id.* Since "[m]ost insurers cannot afford to drop their commercial writings," they "are forced to absorb the losses imposed by restrictive auto insurance regulation." *Id.*

The FAIR Act is perhaps the most restrictive scheme of state automobile insurance regulation ever adopted, and has significantly increased the already substantial burdens borne by New Jersey insurers. Even before passage of the FAIR Act, New Jersey's auto insurance market was persistently unprofitable because regulators had artificially suppressed rate levels. As a New Jersey insurance official candidly explained, "New Jersey has used tight controls on auto rates to avoid paying the actual cost of the state's high accident rate and unbalanced no-fault system. As a result, the voluntary market has been unprofitable. . . ." Special Deputy Insurance Commissioner David N. Grubb, *Solving the Auto Insurance Crisis in New Jersey*, Apr. 10, 1989, at 3 (executive summary). Due to this rate suppression, the New Jersey Department of Insurance has found that "insurers

have lost money on private passenger auto in New Jersey in 10 out of 13 years. . . . In fact, over the 13-year period [from 1976 to 1989], operating losses on auto insurance have been more severe in New Jersey than in any other state." *Insurance Profitability Report*, The Insurance Reporter (N.J. Dept. of Insurance), Nov. 1989, at 2.

Passage of the FAIR Act in 1990 substantially amplified these regulatory burdens in the following respects:

—In 1983, New Jersey had created the New Jersey Automobile Full Insurance Underwriting Association (the "JUA") to provide coverage for automobile drivers otherwise unable to obtain it. All insurers were required to participate in the JUA and thus were jointly obligated to underwrite the state's riskiest drivers. However, the 1983 statute protected the JUA's member companies from incurring losses as a result of this state mandate. Insurers were exempted from liability for JUA deficits, which were made the state's responsibility. In addition, JUA rates, including surcharges on voluntary market policyholders, were required to be set at levels permitting the JUA to operate on a break-even basis. *See* N.J. Stat. Ann. §§ 17:30E-2, -7(b), -7(c), -8(a) (1983). In fact, however, rates were not set at adequate levels and, by 1990, the JUA had "accumulated a deficit of over $3.3 billion in unpaid claims and other losses." *State Farm v. State*, 590 A.2d 191, 196 (N.J. 1991).

In 1990, the FAIR Act repudiated the state's promise that insurers would not be liable for any JUA deficit. Insurers were required to pay for the bulk of JUA losses, through premium surtaxes and nonrepayable "loans" to a state fund. *See id.* at 196-97. New Jersey's Supreme Court rejected a facial constitutional challenge to these taxes and assessments as confiscatory, ruling that the Insurance Commissioner must afford carriers rate increases to recoup the added costs if they would deprive insurers of the opportunity to earn a fair return on

investment. *See id.* at 206-07. To date, however, the Insurance Commissioner has refused to permit any pass-through of these levies even though they have been imposed since 1990. *See, e.g., In re Private Passenger Automobile Rate Filings On Behalf Of State Farm Mutual Automobile Insurance Concerning FAIR Act Surtaxes and Assessments*, Ins. Dept. Order No. A92-319 (Nov. 17, 1992). The resulting losses can never be recovered because New Jersey's prospective ratemaking system permits recovery only of future estimated expenses, not past losses. *See Elizabethtown Water Co. v. New Jersey Bd. of Pub. Utils.*, 527 A.2d 354 (N.J. 1987).

—In 1988, New Jersey sought gradually to phase out the JUA through a statutory "depopulation" program by which policyholders were transferred from the "residual" market into the private or "voluntary" market. In 1990, to facilitate this transition, the FAIR Act created a Market Transition Facility ("MTF") for providing interim coverage to residual market risks prior to the completion of the depopulation program. *See* N.J. Stat. Ann. § 17:33B-11 (1990). As in the case of the predecessor JUA, MTF rates were to be calculated to permit break-even operation. *See In re Commissioner of Ins.*, 606 A.2d 851 (N.J. Super. Ct. App. Div. 1992), *cert granted*, 611 A.2d 653 (N.J. 1992). However, the Commissioner once again failed to set rates adequate to protect against losses, and as a result, the MTF accumulated a deficit in excess of $375 million in the first year of its existence. A New Jersey state court found that the Commissioner's refusal to operate the MTF on a no-loss basis violated the FAIR Act, *see id.*, but the Commisioner nevertheless has recently taken steps to assess the MTF deficit against insurers.

—The FAIR Act also substantially eliminated New Jersey's "voluntary" auto insurance market. Formerly, insurers could decline to underwrite drivers that did not meet individual company underwriting criteria. Now,

however, under the FAIR Act's "depopulation" program and so-called "take all comers" provision, insurers are obligated to accept all risks except drivers with the very worst record of traffic offenses.

Under the "depopulation" program, insurers must "voluntarily" underwrite JUA and MTF risks, or else those drivers will be assigned to them by the Commissioner. *See* N.J. Stat. Ann. § 17:30E-14. The "take all comers" provision then requires insurers to continue to accept former JUA and MTF risks, by forbidding insurers from turning down virtually any customer that approaches them. *See* N.J. Stat. Ann. § 17:33B-15. Once accepted, another statutory provision compels insurers to renew the policies of existing insureds, except on the basis of serious traffic offenses. *See* N.J. Stat. Ann. § 17:33B-25. In effect, New Jersey has converted private insurers into public utilities having a common carrier obligation.

The constitutionality of the above provisions is not presented for decision in this case. The issue, rather, is whether insurers have a right to leave a market in response to the imposition of such measures, especially when the measures fundamentally change the regulatory environment upon which companies relied in making their investments.

Regardles of whether these measures are constitutional, they undeniably impose novel and substantial burdens. The court below admitted as much by noting that the FAIR Act "unquestionably renders more burdensome and less profitable the private-passenger automobile-insurance business in New Jersey." Pet. App. A-19. Nevertheless, the lower court flatly ruled that petitioners were not denied substantive due process when New Jersey sought to prevent avoidance of "the remedial burdens imposed by the Act" by prohibiting withdrawal from the market. Pet. App. A-18.

This ruling conflicts with the reasoning of many lower federal court decisions which have addressed federal and

state regulatory laws that, like the FAIR Act, severely limit a company's opportunity to earn a fair return on investment. These decisions have implicitly viewed the right of withdrawal from the regulated market as an essential safeguard against regulatory overreaching. *See, e.g., Whitney v. Heckler*, 780 F.2d 963, 972 (11th Cir.) ("[G]overnment price regulation does not constitute a taking of property where the regulated group is not required to participate in the regulated industry."), *cert. denied*, 479 U.S. 813 (1986); *Minnesota Ass'n of Health Care Facilities v. Minnesota Dep't. of Pub. Welfare.*, 742 F.2d 442, 446 (8th Cir. 1984) (regulation of nursing home fees was not a "taking" because "nursing homes, unlike public utilities, have freedom to decide whether to remain in business and thus subject themselves voluntarily to the limits imposed by Minnesota on the return they obtain from investment of their assets"), *cert. denied*, 469 U.S. 1215 (1985); *MAPCO, Inc. v. Carter*, 573 F.2d 1268, 1282 (Temp. Emer. Ct. App.) (crude oil price controls were not unconstitutional because they did not "deprive the plaintiffs of the right to withdraw from the market"), *cert. denied*, 437 U.S. 904 (1978).

Here, New Jersey has eliminated this constitutional safety valve against onerous regulation. This case thus squarely presents a question on which the lower courts have been divided and which has not yet been addressed by this Court: Does the Due Process Clause afford insurers a liberty interest in withdrawing from a market when a state imposes new types of regulation that upset settled investment expectations?

II. THE DECISION BELOW SHOULD BE REVIEWED TO DETERMINE THE APPLICATION OF THE UNCONSTITUTIONAL CONDITIONS DOCTRINE TO LAWS DETERRING MARKET WITHDRAWAL BY THREATENING CONFISCATION OF PROPERTY INTERESTS IN AN UNRELATED BUSINESS.

This case also presents the question whether a state may seek to block such withdrawal through the imposition of an unconstitutional condition. This issue should be reviewed for two reasons: (1) to resolve the uncertainty over the application of this Court's decisions to a state's attempt to further its regulatory interests in one economically distinct market by threatening the seizure of valuable property in a separate market; and (2) to resolve conflicting decisions by the highest courts of Massachusetts, New Jersey, and North Carolina on the applicability of the unconstitutional conditions doctrine to insurance "lock-in" laws.

A. This Court Has Not Spoken Definitively on a State's Power to Condition Access to a Profitable Market on Participation in an Unrelated, Unprofitable Market.

This case implicates the unconstitutional conditions doctrine in two ways. First, because Twin City and its affiliates had a property right in their insurance licenses,[2] the Commissioner's license forfeiture order required petitioners to remain in the personal auto insurance market on pain of losing valuable property interests in other

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[2] The court below described the "property affected by the regulation [as] the value of the Twin City affiliates' New Jersey insurance business." Pet. App. at A-28. This description of the petitioners' property interests accurately describes New Jersey law, which regards the holder of a license as having a property right. *See Herz v. Degnan*, 648 F.2d 201, 208 (3d Cir. 1981), and cases cited in Pet. at 23. Hence, the state cannot constitutionally revoke insurance licenses for impermissible or purely arbitrary reasons.

markets. Second, if, as AIA believes, Twin City had a protected liberty interest in exiting the New Jersey auto insurance market, the Commissioner's order required petitioners to forfeit a due process right as a condition of retaining non-automobile insurance licenses. Either way, this Court's decisions indicate, without explicitly holding, that the conditions imposed by the Commissioner are constitutionally valid only if the interests being pursued by New Jersey in one insurance market are legitimately connected to the benefits conferred on insurers by the state-granted license or withdrawal right in the second insurance market.

Until passage of the 1990 "lock-in" law, New Jersey's regulatory regime recognized no such valid linkage between the benefits of engaging in non-automobile insurance businesses and the burdens associated with the auto insurance business, or vice versa. The state rightly treated these different lines of insurance as entirely separate businesses. The authorization to engage in one line was never conditioned on selling a separate line. There is no cross-subsidization between these different markets. Rates for each market are set separately, based on the costs associated with that market, and losses in one line of insurance cannot be offset through rate increases in a separate line. Thus, a company's departure from the automobile insurance market does not in any way burden other property and casualty markets and, conversely, an insurer's continuing participation in non-automobile insurance markets has no effect on the automobile market.

The only linkage between these markets cited by the court below and by the Commissioner is that threatening to seize profitable non-automobile insurance businesses will "encourage" insurers to remain in the unprofitable automobile insurance market. Pet. App. A-87. Hence, the requirement that petitioners forfeit their right to engage in non-auto insurance business is admittedly unrelated to furthering any state interest in those markets.

The Commissioner is simply using the happenstance of an insurer's profits in unrelated insurance markets as leverage for conscripting them into serving the personal automobile insurance market. Prior decisions of this Court strongly suggest that such coercive use of power over unrelated property interests is not constitutionally permissible.

For example, in *Nollan v. California Coastal Commission*, 483 U.S. 825 (1987), the Court held that it was unconstitutional for a California state agency to condition the grant of a permit to build a house on beachfront property upon the landowner's grant of an easement for public access along the beachfront. The Court's direct holding was that the state's action violated the Takings and Due Process Clauses because the condition demanded (the granting of an easement along the beach on the *oceanfront* side of the house) did not in any way further California's asserted regulatory purpose (prevention of new construction that might block a view of the beach by persons on the *landward* side of the house). In this case, the Commissioner's threatened revocation of non-automobile insurance licenses substantially advances —all too effectively—New Jersey's illegitimate interest in preventing withdrawal of automobile insurers.

But *Nollan* was also premised on the idea that the property interests affected by the state-imposed condition must have some legitimate relationship to the regulatory interests being served. The opinion suggests that the easement condition imposed by California was unconstitutional not merely because it failed to advance the state's claimed interest, but also because the property interest affected by the condition (*i.e.*, the beachfront easement) had no connection to the property supposedly being regulated (*i.e.*, the house) and the state's interests in regulating housing construction. California was simply using its permit power as a coercive device to obtain an unrelated easement or, more bluntly, was engaged in "an out-and-out plan of extortion." 483 U.S. at 837 (citation omitted).

Here, too, New Jersey is using its power over non-automobile insurance licenses as a coercive device to effectuate regulatory interests have nothing whatsoever to do with the property which the state threatens to confiscate. The Commissioner's decision is therefore considerably more far-reaching than that before the Court in *California State Automobile Ass'n. Inter-Insurance Bureau v. Maloney*, 341 U.S. 105 (1951), where the Court upheld a California requirement that auto insurers underwrite certain undesirable auto insurance risks, on pain of losing their licenses *in the auto insurance market. See id.* at 108.

The Commissioner's decision does not equitably condition the benefits of engaging in one business on assuming regulatory burdens in that same business. Rather, to compel the assumption of burdens in the automobile insurance market, he is threatening to withhold a privilege conferring benefits in other markets that have no relationship to the burdens he seeks to impose. Indeed, the license forfeiture condition affects Twin City affiliates that are not in the auto insurance business at all. The Commissioner's action is scarcely different than threatening the petitioners that, if they withdraw from the unprofitable automobile insurance market, the state will seize the profitable hotel and manufacturing businesses owned by their parent company, the ITT Corporation.

The rationale of the *Nollan* decision strongly indicates that a state cannot threaten the seizure of an unrelated property interest to coerce compliance with a regulatory requirement having no nexus whatsoever with the property being confiscated. A writ of *certiorari* should be issued to clarify the applicability of *Nollan* and predecessor cases to attempts by state regulators to pursue state regulatory interests in one market by threatening confiscation of property interests in separately regulated markets.

B. State Supreme Courts Have Issued Conflicting Decisions on Whether a State May Permissibly Condition Withdrawal From One Insurance Market on Forfeiture of Licenses in Others.

Review of the decision below is especially needed because state courts have rendered inconsistent decisions on the constitutionality of lock-in laws generally and on the applicability of the unconstitutional conditions doctrine to such laws specifically.

The decision below is consistent with the earlier decision of the Massachusetts Supreme Judicial Court in *Maryland Casualty Co. v. Commissioner of Insurance*, 363 N.E.2d 1087 (Mass. 1977). That case involved a "lock-in" law closely similar to the New Jersey statute. If the Massachusetts Commissioner of Insurance determined that a withdrawing automobile insurer would "disrupt[] the market for said insurance . . . [and that such withdrawal] is not justified by the protection of solvency and is contrary to the public interest, he shall suspend such company's licenses to issue or sell any other form of insurance within the commonwealth." Mass. Gen. L. ch. 175, § 22H. The Massachusetts court, consistently with the New Jersey Supreme Court, rejected arguments that this license forfeiture condition was "confiscatory" and "a deprivation of liberty." 363 N.E.2d at 1099.

A North Carolina Supreme Court decision is directly to the contrary. In *Hartford Accident & Indemnity Co. v. Ingram*, 226 S.E.2d 498 (N.C. 1976), the court considered a statute conditioning an insurer's retention of its license to write general liability insurance on a requirement that it also underwrite medical malpractice insurance. Relying on the venerable line of unconstitutional conditions cases, the court ruled that the state could not, "as a condition precedent to the right of the plaintiffs to retain their licenses to engage in the business of insuring against liability for personal injury or property damage from other risks, require them to enter into the entirely separate and distinct business of insuring against liability for personal injury resulting from the practice of medicine." 226 S.E.2d at 507.

The New Jersey and Massachusetts decisions are also in conflict with a New York State decision. In *People ex rel. Lewis v. Safeco Insurance Co. of America*, 414 N.Y.S.2d 823 (1978), the New York Supreme Court held that the attempt of the Superintendent of Insurance to require two insurers to remain in the state violated due process: "Absent the most severe and grave public emergency, the State may not compel a corporation to conduct a business against its choosing." *Id.* at 830.

Unless this conflict is resolved, state legislators, regulators and insurers will face continuing uncertainty whether other states can follow New Jersey's lead and enact insurance "lock-in" laws.[3]

III. THE COURT SHOULD DETERMINE WHETHER STATE LAWS HOLDING INSURERS CAPTIVE TO LOCAL MARKETS SERVE AN ILLEGITIMATE PROTECTIONIST PURPOSE.

This case also presents the important question whether onerous penalties on withdrawal from state markets serve an illegitimate protectionist interest that violates the Due Process Clause.

The New Jersey Supreme Court forthrightly described the license forfeiture provision of the FAIR Act as having a protectionist purpose: "In such a period of regulatory turmoil and uncertainty, nothing short of severe regulatory measures imposed on private-passenger insurers threatening to withdraw—in other words, strong medicine —would be effective. If the forfeiture condition discourages withdrawal, a substantial State interest—retention of private-passenger insurers—will have been advanced." Pet. App. A-20. In effect, the lower court acknowledged that New Jersey was conscripting the capital of Twin

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[3] In the period since the enactment of the New Jersey FAIR Act, several state legislatures already have considered bills to create lock-in regimes akin to New Jersey's. *See, e.g.*, Maine S. 228 (1991); Maryland S. 698 (1991); Rhode Island H. 8333 (1992); Rhode Island H. 7519 (1992); Vermont H. 130 (1991).

City to serve the interests of local policyholders by depriving the company of its freedom to move its resources elsewhere in interstate commerce.

Indeed, New Jersey's "lock-in" law discriminates against interstate commerce in three respects. First, it requires "business operations to be performed in the home State that could more efficiently be performed elsewhere." *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 145 (1970). Like laws requiring a business to locate its operations within a particular state, "lock-in" laws "impose . . . a straitjacket on [a] company with respect to the allocation of its interstate resources." *Id.* at 146.

Second, since the New Jersey automobile insurance market is unprofitable, the "lock-in" law requires insurers to subsidize a local market out of the pockets either of its customers in other states or its shareholders. Because New Jersey prohibits its insurers from raising their rates in non-automobile insurance markets to recover automobile insurance losses, New Jersey insureds in non-automobile insurance markets do not bear any part of the burden of automobile market losses. Multi-state insurers operating in New Jersey must either pass those losses through to their shareholders, in the form of reduced earnings and dividends, or to their policyholders in other states.

Third, as even the lower court seemed to concede, a "lock-in" law eliminates "competition among state governments [that] tends to prevent overregulation, [by] offering companies choices in determining those States' regulatory systems to which it will subject its business operations." Pet. App. A-28.

Because of this discrimination against interstate commerce, in any other industry, the Commerce Clause would prohibit lock-in laws. Laws requiring a business to remain in-state are "virtually *per se* illegal," even "where the State is pursuing a clearly legitimate local interest." *Pike v. Bruce Church, Inc.*, 397 U.S. at 145; *see also*

South-Central Timber Dev., Inc. v. Wunnicke, 467 U.S. 82 (1984); *Toomer v. Witsell*, 334 U.S. 385, 403-06 (1948); *Foster-Fountain Packing Co. v. Haydel*, 278 U.S. 1 (1928).

Even though the McCarran-Ferguson Act, 15 U.S.C. § 1011 *et seq.*, "removed all Commerce Clause limitations on the authority of the States to regulate and tax the business of insurance," *Western & S. Life Ins. Co. v. State Bd. of Equalization*, 451 U.S. 648, 653 (1981), state laws creating obstacles to the free flow of interstate commerce may still be invalid under other constitutional provisions if they have a protectionist purpose. This is particularly true when, as here, a state attempts to effectuate its protectionist intent by "impos[ing] *unconstitutional* conditions on the grant of [the] privilege" of doing business in that state. *Id.* at 657-58 (emphasis in original).

In *Metropolitan Life Insurance Co. v. Ward*, 470 U.S. 869 (1985), the Court struck down an Alabama insurance tax law under the Equal Protection Clause because it had an illegitimate protectionist goal. The Court concluded that a purpose to promote the interests of domestic insurance companies was illegitimate when the goal was not to advance "the *interstate* business" of those local companies but, rather, "to favor domestic industry within the State, no matter what the cost to foreign corporations also seeking to do business there." *Id.* at 877, 878 (emphasis in original).

While the Commerce Clause may not apply in this context, New Jersey's protectionist action here, like the Alabama statute struck down in *Metropolitan Life*, violates a separate constitutional provision (the Due Process Clause) that clearly does apply in the insurance context. New Jersey's "lock-in" law is the mirror image of the statute struck down in *Metropolitan Life*. Rather than "erect[ing] barriers to foreign companies who wish to do

interstate business" within the state, *id.* at 878, New Jersey is erecting barriers to companies doing business within New Jersey who wish to do additional business outside the state by preventing them from reallocating their resources beyond the state's borders. The fact that New Jersey has created a market exit barrier rather than an entry barrier is thus immaterial because, in both cases, the purpose is to protect a local market by creating obstacles to the free flow of interstate commerce. Like Alabama's objective, New Jersey's aim is "to favor domestic [policyholders] within the State, no matter what the cost to foreign [policyholders.]" 470 U.S. at 878.

The state court decision below should thus be reviewed because, like the decision of the Alabama Supreme Court scrutinized in *Metropolitan Life*, it presents an important question concerning whether protectionist state insurance laws serve a constitutionally permissible state interest.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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